GENUITY INC.

INDEX TO COMBINED FINANCIAL STATEMENTS

After the recapitalization, issuance of Class B common stock and finalization of agreements discussed in Note 14 to Genuity Inc.'s combined financial statements are effected, we expect to be in a position to render the following audit report.

ARTHUR ANDERSEN LLP

April 7, 2000

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Board of Directors and Shareholder of Genuity Inc.:

We have audited the accompanying combined balance sheets of Genuity Inc. (comprised of certain operations of GTE Internetworking Incorporated and wholly-owned by GTE Corporation) (the Company) as of December 31, 1998 and 1999, and the related combined statements of operations, changes in stockholder's equity, cash flows and comprehensive loss for each of the three years in the period ended December 31, 1999. We have also audited the statements of operations, changes in shareholder's equity, cash flows and comprehensive loss of the Company's predecessor for the six months ended June 30, 1997, the period prior to the acquisition by the Company. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 1998 and 1999, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 1999 and the results of operations and cash flows of the Predecessor for the six months ended June 30, 1997 in conformity with accounting principles generally accepted in the United States.

Our audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplemental schedule is presented for purposes of complying with the Securities and Exchange Commission's rules and is not part of the basic financial statements. This schedule has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, fairly states in all material respects the financial data required to be set forth therein in relation to the basic financial statements taken as a whole.

Boston, Massachusetts
, 2000

GENUITY INC.

COMBINED STATEMENTS OF OPERATIONS

(dollars in thousands, except per share data)

	Predecessor	Genuity		
	Six Months Ended June 30, 1997	Year Ended December 31,		
		1997	1998	1999
Revenues				
Access	$ 94,126	$ 128,838	$ 350,777	$ 574,503
Hosting	9,601	9,690	33,469	48,811
Transport	—	65,221	72,412	89,541
Other	2,591	3,035	14,880	37,569
Total revenues	106,318	206,784	471,538	750,424
Operating Expenses				
Cost of goods sold	92,670	184,914	512,967	786,965
Selling, general and administrative	38,801	144,360	316,491	399,529
Depreciation and amortization	10,536	49,483	104,523	188,667
Total operating expenses	142,007	378,757	933,981	1,375,161
Operating Loss	(35,689)	(171,973)	(462,443)	(624,737)
Other Income (Expense)				
Interest expense, net	(478)	(1,346)	(20)	(183)
Other, net	(1,496)	1,814	(2,924)	(32)
Loss Before Income Taxes	(37,663)	(171,505)	(465,387)	(624,952)
Income Taxes	—	535	1,653	1,737
Net Loss	$(37,663)	$(172,040)	$(467,040)	$(626,689)
Basic and Diluted Loss Per Common Share	$( )	$( )	$( )	$( )
Basic and Diluted Weighted-Average Common Shares Outstanding				

See notes to combined financial statements.

GENUITY INC.

COMBINED BALANCE SHEETS
(dollars in thousands)

	December 31, 1998	December 31, 1999
Assets		
Current Assets:		
Cash and cash equivalents	$ 13,883	$ 6,044
Receivables, less allowances of $3,651 and $5,550	150,630	217,649
Receivables—affiliates	18,077	40,462
Note receivable—affiliate	33,574	—
Other current assets	19,099	13,627
Total current assets	235,263	277,782
Property, Plant and Equipment, Net	908,039	1,524,390
Goodwill and Other Intangibles, Net	556,435	542,876
Other Assets	3,724	28,111
Total assets	$1,703,461	$2,373,159
Liabilities and Stockholder's Equity		
Current Liabilities:		
Short-term obligations, including current maturities	$ 20,499	$ 25,921
Note payable—affiliate	—	126,503
Accounts payable	73,711	142,752
Accounts payable—affiliates	13,440	38,647
Accrued compensation and related liabilities	15,763	49,637
Accrued circuits	—	44,786
Accrued liabilities	41,008	81,696
Advanced billings	10,172	26,320
Total current liabilities	174,593	536,262
Long-Term Obligations	126,855	112,717
Employee Benefit Plan Obligations and Deferred Compensation	46,388	20,466
Other Liabilities	3,406	370
Total long-term liabilities	176,649	133,553
Stockholder's Equity:		
Class B common stock—$ par value shares issued and outstanding	—	—
Additional paid-in capital	2,004,380	2,983,426
Other comprehensive income	3,928	2,696
Accumulated deficit	(656,089)	(1,282,778)
Total stockholder's equity	1,352,219	1,703,344
Total liabilities and stockholder's equity	$1,703,461	$2,373,159

See notes to combined financial statements.

GENUITY INC.

COMBINED STATEMENTS OF CASH FLOWS
(dollars in thousands)

	Predecessor	Genuity		
	Six Months Ended June 30,	Year Ended December 31,		
	1997	1997	1998	1999
Cash flows from operating activities:				
Net loss	$(37,663)	$(172,040)	$ (467,040)	$ (626,689)
Adjustments to reconcile net loss to net cash provided by (used in) operations:				
Depreciation and amortization	10,536	49,483	104,523	188,667
Changes in current assets and current liabilities:				
Receivables—net	(15,602)	(24,289)	(76,723)	(89,404)
Other current assets	726	(9,020)	(6,730)	5,472
Other current liabilities	46,265	104,761	(82,421)	175,160
Other, net	(1,766)	(28,467)	26,823	(52,495)
Net cash provided by (used in) operating activities	2,496	(79,572)	(501,568)	(399,289)
Cash flows from investing activities:				
Capital expenditures	(2,830)	(255,903)	(505,303)	(672,030)
Purchase of businesses, net of cash acquired	—	(517,788)	—	—
Other, net	—	—	—	(36,244)
Net cash used in investing activities	(2,830)	(773,691)	(505,303)	(708,274)
Cash flows from financing activities:				
Repayment of long-term debt	(34,012)	(11,363)	(29,547)	(37,512)
Change in short-term obligations	10,249	346	9,904	5,422
Change in note payable/receivable—affiliate	—	256,352	(289,926)	160,077
Contributions from GTE	—	610,688	1,327,260	971,737
Net cash provided by (used in) financing activities	(23,763)	856,023	1,017,691	1,099,724
Net increase (decrease) in cash and cash equivalents	(24,097)	2,760	10,820	(7,839)
Cash and cash equivalents, beginning of period	102,870	303	3,063	13,883
Cash and cash equivalents, end of period	$ 78,773	$ 3,063	$ 13,883	$ 6,044
Supplemental Cash Flows Disclosure				
Cash paid during the year for:				
Interest	$ 671	$ 2,142	$ 16,401	$ 4,403
State income taxes	$ —	$ 535	$ 1,653	$ 1,737
Noncash Investing and Financing Activities:				
Capital lease obligation incurred for equipment purchase	$ 20,425	$ 21,469	$ 54,958	$ 23,374
Accounts payable—work in process	—	$ 22,119	$ 27,570	$ 54,584

See notes to combined financial statements.

GENUITY INC.

COMBINED STATEMENTS OF
CHANGES IN STOCKHOLDER'S EQUITY
(dollars in thousands)

	Common Stock	Additional Paid-In Capital	Accumulated Deficit	Other Comprehensive Income (Loss)	Treasury Shares	Total
PREDECESSOR						
Balance, December 31, 1996	$25,041	$ 115,456	$ (5,967)	$ —	$(28,419)	$ 106,111
Stock option exercises	88	1,912	—	—	—	2,000
Conversion of debentures	249	7,562	—	—	—	7,811
Net loss	—	—	(37,663)	—	—	(37,663)
Other	—	—	—	(1,033)	—	(1,033)
Balance, June 30, 1997	$25,378	$ 124,930	$ (43,630)	$(1,033)	$(28,419)	$ 77,226
GENUITY						
Balance, December 31, 1996	$ —	$ 47,764	$ (17,009)	$ —	$ —	$ 30,755
Conversion of Predecessor equity instruments	—	16,186	—	—	—	16,186
Capital contributions—GTE	—	610,688	—	—	—	610,688
Net loss	—	—	(172,040)	—	—	(172,040)
Other	—	—	—	2,046	—	2,046
Balance, December 31, 1997	—	674,638	(189,049)	2,046	—	487,635
Tax benefit on exercise of stock options—GTE	—	2,482	—	—	—	2,482
Capital contributions—GTE	—	1,327,260	—	—	—	1,327,260
Net loss	—	—	(467,040)	—	—	(467,040)
Other	—	—	—	1,882	—	1,882
Balance, December 31, 1998	—	2,004,380	(656,089)	3,928	—	1,352,219
Tax benefit on exercise of stock options—GTE	—	7,309	—	—	—	7,309
Capital contributions—GTE	—	971,737	—	—	—	971,737
Net loss	—	—	(626,689)	—	—	(626,689)
Other	—	—	—	(1,232)	—	(1,232)
Balance, December 31, 1999	$ —	$2,983,426	$(1,282,778)	$ 2,696	$ —	$1,703,344

See notes to combined financial statements.

GENUITY INC.

COMBINED STATEMENTS OF COMPREHENSIVE LOSS
(dollars in thousands)

	Predecessor	Genuity		
	Six Months Ended June 30, 1997	Year Ended December 31,		
		1997	1998	1999
Net Loss	$(37,663)	$(172,040)	$(467,040)	$(626,689)
Other Comprehensive Income (Loss):				
Foreign currency translation adjustments	(113)	(37)	32	118
Unrealized gain (loss) on securities	(920)	2,083	1,850	(1,350)
	(1,033)	2,046	1,882	(1,232)
Comprehensive Loss	$(38,696)	$(169,994)	$(465,158)	$(627,921)

See notes to combined financial statements.

GENUITY INC.

NOTES TO COMBINED FINANCIAL STATEMENTS
December 31, 1997, 1998 and 1999

1. Description of Business and Summary of Significant Accounting Policies:

Description of Business and Organization

Genuity Inc. (Genuity or the Company), a Delaware corporation, is a wholly-owned subsidiary of GTE Corporation (GTE). Genuity is a leading facilities-based provider of managed Internet infrastructure services. By leveraging a technologically advanced, high-bandwidth global fiber-optic network, data center facilities, and a rapidly growing base of business and consumer users and content directly attached to its Internet backbone, Genuity engineers and delivers a comprehensive suite of managed Internet infrastructure services. These services include Internet access through dial-up, dedicated and digital subscriber lines; web hosting and content delivery; and value added e-business services, such as virtual private networks for secure data transmission, security services and voice-over-IP. Genuity's services are provided to both enterprises and service providers including Internet service providers, application service providers and carriers.

Genuity's predecessor incurred net losses of $37.7 million for the six months ended June 30, 1997. Genuity incurred net losses of $172.0 million, $467.0 million and $626.7 million for the years ended December 31, 1997, 1998 and 1999, respectively. To date, Genuity has incurred cumulative operating losses of $1,282.8 million. Given the level of planned operating and capital expenditures, Genuity expects to continue to incur significant operating losses for the next several years.

The markets in which Genuity operates can be characterized as rapidly changing due to technological developments, evolving industry standards and customer demands and frequent new product and service introductions and enhancements. Genuity expects to continue to make significant investments to expand its capacity and facilities infrastructure, develop brand recognition, broaden the range of service offerings and expand its sales, marketing, technical and customer support personnel. These efforts will require significant expenditures, a substantial portion of which will be made before any significant corresponding revenue may be realized.

Genuity is also dependent on a limited source of suppliers for a number of components and parts necessary for its network buildout and operations. Genuity does not carry significant inventories of components and has no guaranteed supply arrangements with vendors. Shortages from these suppliers could cause significant delays in or abandonment of the expansion of the network and could have an adverse affect on Genuity's operating results.

Basis of Presentation

The accompanying combined financial statements of Genuity include the financial position of some of the operations of GTE Internetworking as of December 31, 1998 and 1999 and results of their operations for each of the three years in the period ended December 31, 1999. Certain of the operations and assets included in these combined financial statements were transferred to Genuity on , 2000. GTE acquired BBN Corporation effective June 30, 1997. This acquisition was accounted for as a purchase business combination and, consequently, the results of operations of BBN Corporation, excluding the operations of BBN Technologies (BBNT), which are being retained by GTE, are included in Genuity for the periods after June 30, 1997. The results of operations of our predecessor represent the results of BBN Corporation, excluding the operations of BBNT.

Genuity prepares its combined financial statements in accordance with generally accepted accounting principles, which require that management make estimates and assumptions that affect reported amounts. Actual results could differ from these estimates.

The combined financial statements of Genuity include the accounts of all majority-owned subsidiaries. All significant intercompany amounts have been eliminated.

Revenue Recognition

Revenue is generally recognized when services are rendered or products are delivered to customers. Access, web hosting and transport customers typically sign one or two-year contracts. Access customer contracts provide for monthly-recurring service fees and/or fees based on utilization. Web hosting revenues are derived primarily from monthly fees, usage of bandwidth and monthly server management fees. Transport revenues are based on customer usage of circuit mileage and bandwidth. Other value-added service revenue is generally based on monthly collocation fees or based on usage of service. Billings made or payments received in advance of providing services are deferred until the period these services are provided.

Genuity has contracts with some customers that provide service level commitments. If Genuity does not meet the required service levels, it may be obligated to provide credits, usually in the form of free service for a short period of time. These amounts are accounted for in cost of sales. To date, credits issued under these arrangements for Genuity's failure to meet service level commitments have not been material. During 1999, one of Genuity's vendors experienced failures on its network, which resulted in a disruption to Genuity's customers. Genuity's vendor provided credits to Genuity for the service failure, which Genuity passed on to its customers.

Advertising Costs

Genuity expenses the cost of advertising as incurred. The Predecessor's advertising expense was $5.1 million for the six months ended June 30, 1997. Genuity's advertising expense was $4.6 million, $16.5 million and $21.5 million for the years ended December 31, 1997, 1998 and 1999, respectively. Advertising expense is included as a component of selling expense in the accompanying combined statements of operations.

Income Taxes

Genuity has historically filed its federal income tax return on a consolidated basis with GTE. Upon completion of the initial public offering, Genuity will be deconsolidated from GTE for income tax purposes. Income tax payments and refunds will be determined based on the stand-alone filings of Genuity. The accompanying combined financial statements are presented as if Genuity was a stand-alone company for all periods presented. The Predecessor was part of a stand-alone entity, and its taxes were recorded on that basis.

Genuity and the Predecessor computed their current and deferred income tax expense on a stand-alone basis in accordance with Statement of Financial Accounting Standards (SFAS) No. 109 "Accounting for Income Taxes," which requires recognition of deferred tax liabilities and assets based upon the expected future tax consequences of events that have been included in the financial statements or tax returns. Under this method, deferred tax liabilities and assets are determined based on the difference between the financial statement and tax basis of assets and liabilities using tax rates in effect for the year in which the differences are expected to reverse. A valuation allowance has been established to reflect the likelihood of realization of deferred tax assets.

Genuity has approximately $39 million of net operating losses and $10 million of research credit carryforwards, which are limited in use due to the fact that they were generated by the Predecessor.

Loss Per Common Share

Loss per common share is calculated based on the provisions of SFAS No. 128, ''Earnings per Share.'' Basic loss per common share of the Predecessor was computed by dividing net loss by the weighted-average number of common shares outstanding during the period. The basic loss per share of Genuity was computed based on the number of common shares that were issued in connection with the recapitalization of Genuity, which occurred on . No stock options or awards of the Predecessor were considered in calculating diluted loss per common share as their effect would be antidilutive. Genuity has no potentially dilutive common shares.

Cash and Cash Equivalents

Cash and cash equivalents include investments in short-term, highly liquid securities, which have maturities when purchased of three months or less.

Property, Plant and Equipment

Property, plant and equipment are stated at cost less accumulated depreciation and amortization. Depreciation is computed over the assets' estimated useful lives using the straight-line method. Useful lives used in computing depreciation are as follows: buildings and fixtures—10 to 30 years, communications network—fiber-optic cable—20 to 25 years, communications network—data processing equipment and machinery which include labor and other direct costs—3 to 10 years and furniture—5 to 7 years. Leasehold improvements are amortized over the shorter of the lease period or their estimated useful lives using the straight-line method. Maintenance and repairs are charged to expense as incurred; improvements are capitalized.

When property is sold or retired, the cost of the property and the related accumulated depreciation are removed from the combined balance sheet and any gain or loss on the transaction is included in the accompanying combined statement of operations.

Work in progress represents costs incurred for the build-out and expansion of the network infrastructure and includes engineering costs and capitalized interest. When these assets are placed in service, the costs are recorded in the appropriate property, plant and equipment accounts and depreciation begins.

Genuity leases data communications equipment under a capital lease agreement. The assets and liabilities under the capital lease are recorded at the present value of minimum lease payments. Assets under the capital lease are depreciated over the term of the lease, which is generally 5 years.

Communications network—fiber optic cable primarily includes an indefeasible right of use agreement with Qwest Communications International Inc. at December 31, 1999.

Goodwill and Other Intangibles

Goodwill and other intangible assets pertain to the acquisitions of the Predecessor and the assets of a web hosting business acquired in 1997, and internal use software. Goodwill is being amortized on a straight-line basis over the lesser of 20 years or the period benefited. Other intangible assets include customer bases, trademarks, developed technology and in-place work forces in connection with the acquisitions, and internal use software. Customer bases and in-place work forces are amortized in a manner consistent with historical attrition patterns over 3 to 10 years. Trademarks, developed technology and internal use software are amortized on a straight-line basis over 3 to 10 years.

Software

In March 1998, the American Institute of Certified Public Accountants issued Statement of Position (SOP) 98-1 ''Accounting for the Costs of Computer Software Developed or Obtained for Internal Use.'' Under the provisions of this SOP, effective January 1, 1999, Genuity was required to capitalize and amortize the cost of all internal-use software. Prior to the adoption of SOP 98-1, primarily all software was expensed as incurred. Software expensed in 1997 and 1998 was approximately $17.3 million and $1.4 million, respectively. Capitalized software is amortized over a useful life ranging from 3 to 5 years. Software maintenance costs are expensed as incurred.

Employee Benefit Plans

For periods prior to the initial public offering, Genuity participated in GTE's pension and postretirement health care and life insurance benefit plans. The plans' cost and liability recorded by Genuity are based on Genuity's participation in GTE's plans.

Valuation of Long-Lived Assets

Genuity periodically reviews the values assigned to long-lived assets such as intangibles and property, plant and equipment, to determine whether any impairments exist that are other than temporary. If circumstances indicated that long-lived assets have been impaired, Genuity would estimate gross cash flows for the estimated useful life of the asset, compared to its carrying value. Genuity's management believes that no impairments exist related to its long-lived assets in the accompanying combined balance sheets.

Concentrations of Credit Risk and Significant Customers

Genuity's accounts receivable subject it to credit risk. Genuity performs regular credit evaluations of its customers' financial condition and maintains allowances for potential credit losses. Genuity's risk of loss is limited due to advance billings to some of its customers for services and the ability to terminate service on delinquent accounts. The credit risk is also mitigated by the large number of customers comprising the customer base, with the exception of one large customer, America Online. Revenues from America Online in relation to Genuity's and Predecessor's total revenues were significant. However, the credit risk associated with America Online is mitigated by advance billings and timely collections. The average accounts receivable balance of America Online represented 34% and 44% of Genuity's receivable balance during 1998 and 1999, respectively, while revenues from America Online represented 53% and 52% of Genuity's total revenues for the years ended December 31, 1998 and 1999, respectively.

Genuity has been a supplier of network access services in the United States to America Online since 1995. Genuity entered into a new agreement with America Online effective as of December 31, 1999, pursuant to which America Online has agreed to purchase additional dial-up access services from Genuity for a seven-year term through December 31, 2006. Under the new agreement, America Online has also agreed to purchase managed digital subscriber line and other broadband network access services from Genuity for a five-year term through December 31, 2004. This agreement includes provisions for minimum purchase requirements at fixed monthly fees, subject to market pricing adjustments, service level requirements and termination provisions.

In providing America Online services under the agreement, Genuity is obligated to comply with specified minimum service levels. Either party may terminate the agreement in the event the other party commits a material breach which is not cured within the specified period. In addition, America Online has the right to terminate the agreement in the event of: (1) repeated material breaches by Genuity; (2) a violation of the most favored customer pricing provisions; (3) a total or near total outage of any of the services provided by Genuity that, while lasting fewer than thirty days, is widespread and prolonged; (4) our inability to meet our service level commitments or to expand service availability as required under the agreement; and (5) a change in control other than through this initial public offering. Genuity is also obligated to provide America Online assistance in the twelve months following any termination of the agreement to ensure a smooth transition of services. The agreement provides America Online with a right of first refusal with respect to the sale of our dial-up network access business.

Under a separate agreement with America Online Japan and Genuity's Japanese branch, Genuity has agreed to provide dial-up network access services to America Online in Japan. This agreement also includes minimum purchase requirements on the part of America Online Japan, market pricing adjustments, service level requirements, and termination provisions.

Financial Instruments

Financial instruments include cash and cash equivalents, accounts receivable, equity securities, accounts payable, notes payable and debt. The fair values of financial instruments included in the combined balance sheets, other than long-term debt, closely approximate their recorded values. The recorded values of equity securities equal their fair values based on quoted market prices, and are classified as available-for-sale securities. The securities are included in other current assets in the accompanying combined balance sheets and have a cost of $11.8 million and $3.5 million at December 31, 1998 and 1999, respectively. The estimated fair value of long-term debt based on a debt pricing model was lower than its recorded value as of December 31, 1998 and 1999 by approximately $1.2 million and $6.6 million, respectively.

Comprehensive Loss

Comprehensive loss is the change in equity from transactions and other events and circumstances that are not from owners. Included in other comprehensive income (loss) are foreign currency translation gains and losses and unrealized gains and losses on available-for-sale securities.

Foreign Currency Translation

Assets and liabilities of units operating in foreign countries are translated into U.S. dollars using the exchange rates in effect on the balance sheet date. Results of operations are translated using the average exchange rates prevailing throughout the period. Foreign assets, liabilities and results of operations are not material in all periods presented.

Recent Accounting Pronouncement

On December 3, 1999, the Securities and Exchange Commission issued Staff Accounting Bulletin (SAB) No. 101, "Revenue Recognition in Financial Statements." Genuity is required to adopt this accounting guidance, as amended by SAB No. 101A, no later than the second quarter of 2000. Genuity adopted this accounting in the first quarter of 2000.

2. GTE's Proposed Merger with Bell Atlantic Corporation:

In July 1998, GTE and Bell Atlantic Corporation (Bell Atlantic) agreed to enter into a merger of equals transaction. The new combined company is Verizon Communications (Verizon). Under the terms of the agreement, which was unanimously approved by the boards of directors of both companies and a majority of the shareholders, GTE's shareholders will receive 1.22 shares of Verizon stock for each share of GTE's stock that they own. The merger is subject to regulatory approvals.

Under the Telecommunications Act of 1996, Regional Bell Operating Companies, including the Bell Atlantic local telephone operating companies, and their respective affiliates, are generally prohibited from providing long distance services that originate in any state in which they operate an incumbent local telephone company. These provisions restrict the operations of these companies until they have satisfied a 14-point competitive checklist under Section 271 of the Telecommunications Act of 1996 (Telecommunications Act) and obtained authority from the Federal Communications Commission (FCC) to provide long distance services in the states in which they operate an incumbent local telephone company.

Bell Atlantic is an incumbent local telephone company in 13 states, stretching from Maine to Virginia, and the District of Columbia. Bell Atlantic has obtained the necessary authorization to provide long distance service originating in New York. Because Genuity provides services in Bell Atlantic's region that could be characterized as long distance services, Bell Atlantic and GTE cannot complete their merger until they either (1) receive relief from the Telecommunications Act restrictions for the remaining states in which Bell Atlantic provides local telephone services or (2) implement a structure that complies with the requirements of the Telecommunications Act.

To ensure compliance with the requirements of the Telecommunications Act and to receive FCC approval of their merger, Bell Atlantic and GTE have proposed a structure to the FCC under which (1) GTE will exchange all of the currently outstanding shares of Genuity common stock for shares of Class B common stock and (2) Genuity will make an initial public offering of Class A common stock. As a result, immediately after completion of Genuity's initial public offering, the investors purchasing shares in the initial public offering will own shares of Genuity's Class A common stock possessing 90% of the total voting power of Genuity's capital stock and GTE will own shares of Genuity's Class B common stock possessing 10% of the total voting power of Genuity's capital stock. Genuity's Class B common stock is convertible at any time into shares of Genuity's Class C common stock that represent approximately 82% of Genuity's total capital stock and possess approximately 96% of the total voting power of Genuity's capital stock, in each case before giving effect to any outstanding options to purchase shares of Genuity common stock, the exercise of the underwriters' over-allotment option or other additional issuances of Genuity common stock. If the underwriters over-allotment option is exercised, Genuity's Class B common stock would be convertible into shares of Class C common stock representing 80% of Genuity's total capital stock.

Under the terms of the proposal to the FCC, the shares of Class B common stock held by Verizon must be converted on or prior to 2005, subject to extension. Assuming no additional issuances of Genuity's common stock after completion of this offering, Verizon will control Genuity if and when it converts its Class B common stock into Class C common stock. Subject to limited exceptions, if Verizon is unable to convert its shares of Class B common stock within this time period, it would be required to dispose of those shares.

Bell Atlantic and GTE are required to receive the formal approval of the FCC for the proposed structure.

3. Property, Plant and Equipment, Net

Property, plant and equipment, net was comprised of the following (in thousands):

	December 31,	
	1998	1999
Land	$ 2,356	$ 2,417
Buildings and fixtures	6,654	14,771
Communications network—fiber-optic cable	300,035	481,573
Communications network—data processing equipment and machinery	483,944	732,306
Furniture	11,083	18,653
Leasehold improvements	95,418	164,542
Work in progress	177,607	402,740
Sub-Total	1,077,097	1,817,002
Accumulated depreciation	(169,058)	(292,612)
Total	$ 908,039	$1,524,390

During 1999, Genuity completed its initial buildout of its communications network in the United States. Costs directly related to the network have been capitalized, including amounts associated with the indefeasible rights of use. Genuity commenced depreciation as individual segments were placed in service.

The Predecessor's depreciation expense was $10.5 million for the six months ended June 30, 1997. Genuity's depreciation expense was $18.8 million, $56.3 million and $138.9 million for the years ended December 31, 1997, 1998 and 1999, respectively.

Interest and network engineering costs capitalized as part of property, plant and equipment were as follows (in thousands):

	Predecessor	Genuity		
	Six Months Ended June 30,	For the Year Ended December 31,		
	1997	1997	1998	1999
Network engineering costs	$422	$1,422	$10,263	$23,148
Capitalized interest	—	—	17,700	6,408
Total	$422	$1,422	$27,963	$29,556

4. Goodwill and Other Intangibles, Net

Goodwill and other intangibles, net was comprised of the following (in thousands):

	December 31,	
	1998	1999
Goodwill	$496,192	$496,192
Customer bases	77,000	77,000
Trademarks	34,000	34,000
Developed technology	19,000	19,000
In-place work forces	9,190	9,190
Internal use software	—	36,244
Sub-Total	635,382	671,626
Accumulated amortization	(78,947)	(128,750)
Total	$556,435	$542,876

Genuity's amortization expense was $30.7 million, $48.3 million and $49.8 million for the years ended December 31, 1997, 1998 and 1999, respectively.

5. Debt

Long-term obligations and short-term obligations were as follows (in thousands):

	December 31,	
	1998	1999
6% convertible subordinated debentures	$ 55,903	$ 48,948
Capital leases	70,952	63,769
Total long-term obligations	$126,855	$112,717
Note payable—affiliate	$ —	$126,503
Current portion of capital leases	20,499	25,921
Total short-term obligations	$ 20,499	$152,424

On April 1, 1987, Predecessor issued $84.7 million of 6% convertible subordinated debentures. The 6% convertible subordinated debentures due 2012 may be converted by the bondholders into cash at an exchange ratio of $966.67 for each $1,000 in principal amount of debentures. The debentures are unsecured obligations of Genuity and are subordinated in right of payment to Genuity's senior indebtedness, if any. Debt issuance costs are being amortized over the term of the debentures. The unamortized balance at December 31, 1999 of $0.6 million is included in other assets in the accompanying combined balance sheets.

Genuity is required to contribute to a sinking fund annual payments equal to 5% of the aggregate principal amount issued. The sinking fund was calculated to retire 70% of the original debentures prior to maturity. To date Genuity has purchased and retired debentures with a face value of $37.3 million which has been used to satisfy the annual sinking fund requirements through 2006.

The interest rate on the note payable to/receivable from GTE is based on an intercompany borrowing interest rate established by GTE, which fluctuated between 4.85% and 6.58% in 1997, 5.41% and 6.24% in 1998 and 6.04% and 6.75% in 1999.

Genuity has entered into leasing agreements to finance some equipment acquisitions. The underlying assets serve to collateralize the debt. The borrowings bear interest at effective rates of 5.07% to 9.50% and have terms of 5 years from the date of purchase, with principal and interest payable quarterly in advance. The leases include purchase and renewal options at fair market values. The leases are classified as capital leases in accordance with the provisions of SFAS No. 13, ''Accounting for Leases.''

Assets under capital leases were as follows (in thousands):

	December 31,	
	1998	1999
Data processing equipment	$91,682	$115,056
Accumulated depreciation	(25,936)	(51,792)
Total	$65,746	$ 63,264

6. Stockholder's Equity

Common Stock

The authorized and issued common stock of Genuity is based on the number of common shares that will be issued in connection with the recapitalization of Genuity, which occurred on . In connection with the recapitalization, the 1,000 shares of common stock issued and outstanding were converted to shares of Class B common stock.

Additional Paid-In Capital

Genuity received contributions from GTE of $610.7 million, $1,327.3 million and $971.7 million, for the years ended December 31, 1997, 1998 and 1999, respectively.

Accumulated Other Comprehensive Loss

Accumulated other comprehensive loss includes cumulative foreign currency translation adjustments and the cumulative unrealized loss on investments in securities. The Predecessor's cumulative foreign currency translation adjustment was a loss of $0.1 million as of June 30, 1997 and Genuity's cumulative foreign currency translation adjustment was a gain of $0.1 million as of December 31, 1999. The Predecessor's cumulative unrealized loss on investments in securities was $0.9 million as of June 30, 1997 and Genuity's cumulative unrealized gain on investments in securities was $2.1 million, $3.9 million and $2.6 million as of December 31, 1997, 1998 and 1999, respectively.

7. Stock-Based Compensation

GTE maintains broad-based stock option plans that has historically covered substantially all Genuity employees. Genuity employees will not participate in these plans after the initial public offering. Prior to 1997, options were granted separately or in conjunction with stock appreciation rights (SARs). Beginning in 1997, the granting of SARs was discontinued. In 1997, GTE's shareholders approved the GTE Corporation 1997 Long-

Term Incentive Plan (the LTIP). Each option granted under the LTIP conveys the right to purchase, at fair market value on the date of the grant, shares of GTE common stock. Generally, options have a term of 10 years and become vested over a period not to exceed three years. At December 31, 1999, 1,595,984 options granted to Genuity employees were exercisable in shares of GTE common stock. Options granted under the Predecessor's stock incentive plan were converted into GTE options or plan participants received cash.

In 1995, the FASB issued SFAS No. 123, ''Accounting for Stock-Based Compensation.'' As permitted by SFAS No. 123, GTE continues to apply the recognition and measurement provisions of Accounting Principles Board Opinion (APB) No. 25, ''Accounting for Stock Issued to Employees.'' In accordance with APB No. 25, compensation expense is not recognized for stock options on the date of grant since it is GTE's practice to grant options with an exercise price equal to the fair market value of its common stock on the date of grant. Under SFAS No. 123, compensation cost is measured at the grant date based on the value of the award and is recognized over the service or vesting period. Had compensation cost for GTE's stock options been determined under SFAS No. 123, based on the fair market value at the grant dates, pro forma net loss and basic loss per share of Genuity would have been as follows (in thousands except per share amounts):

	Genuity		
	For the Year Ended December 31,		
	1997	1998	1999
Net loss			
As reported	$(172,040)	$(467,040)	$(626,689)
Pro forma	(173,055)	(472,845)	(648,201)
Basic and diluted loss per share			
As reported	$ ( )	$ ( )	$ ( )
Pro forma	( )	( )	( )

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model with the following weighted-average assumptions for GTE options granted during the years ended December 31, 1997, 1998 and 1999: expected volatility of 18%-19.5%, expected maturities of seven years, risk-free interest rates equal to the yield on seven-year U.S. Treasury notes on the grant date and expected dividend yield of approximately 3%.

8. Employee Benefit Plans

Genuity does not intend to offer a pension or other postretirement plan to employees once its employees are no longer employees of GTE. Genuity does intend to offer a defined contribution (401(k)) plan.

GTE sponsors several qualified and nonqualified pension plans and other postretirement benefit plans for its employees, which prior to the initial public offering, include Genuity's employees. The Predecessor did not sponsor either a pension plan or an other postretirement benefit plan. Approximately 600 of Genuity's employees are covered under defined benefit pension plans and postretirement health care and life insurance plans. Pension plans are generally noncontributory by plan participants. Postretirement health care plans are generally contributory and include a limit on the portion of the cost of benefits for recent and future retirees paid by Genuity.

The cost and liability for the pension and other postretirement benefit plans recorded by Genuity are based on Genuity's participation in GTE's plans, representing an allocation of the GTE's plans' assets and liabilities. Genuity's pension expense was $0.5 million, $0.9 million and $2.6 million for the years ended December 31, 1997, 1998 and 1999, respectively. Genuity's other postretirement benefit expense was $0.2 million, $0.4 million and $0.3 million for the years ended December 31, 1997, 1998 and 1999, respectively. Genuity's pension liability was $2.5 million and $5.1 million as of December 31, 1998 and 1999, respectively. Genuity's other postretirement benefit liability was $2.0 million and $2.2 million as of December 31, 1998 and 1999, respectively.

GTE sponsors employee savings and stock ownership plans under section 401(k) of the Internal Revenue Code. Through the date of the initial public offering the plans cover substantially all full-time employees of Genuity. Under the plans, Genuity provides matching contributions in either cash or GTE common stock based on qualified employee contributions. Genuity's matching contributions charged to income were $1.0 million, $3.1 million, and $4.8 million for the years ended December 31, 1997, 1998 and 1999, respectively.

BBN Corporation maintained the BBN Corporation Retirement Trust Agreement, which is a 401(k) plan that includes matching and profit sharing features. The plan covers most employees of Genuity who are not covered by the GTE Savings Plan. It is anticipated that the plan will be sponsored and maintained by Genuity or one of its affiliates after the offering. The Predecessor's matching contribution charged to income was $0.6 million for the six months ended June 30, 1997.

9. Interest Expense, Net

The combined statements of operations reflect total interest expense, less interest capitalized during construction and interest income as follows (in thousands):

	Predecessor	Genuity		
	Six Months Ended June 30,	Year Ended December 31,		
	1997	1997	1998	1999
Interest expense	$(2,951)	$(1,346)	$(17,720)	$(9,952)
Interest capitalized	—	—	17,700	6,408
Interest income	2,473	—	—	3,361
Total	$ (478)	$(1,346)	$ (20)	$ (183)

10. Income Taxes

The income tax accounts included in the accompanying combined balance sheets and statements of operations are presented as if Genuity were a stand-alone company for all periods presented. The Predecessor was part of a stand-alone entity, and its income taxes were recorded on that basis. Taxable losses of Genuity aggregating $111.3 million, $524.4 million and $636.7 million for the years ended December 31, 1997, 1998 and 1999, respectively, have been benefited to GTE in its consolidated tax return. Genuity received reimbursements aggregating $39.2 million, $184.9 million and $222.8 million for the years ended December 31, 1997, 1998 and 1999, respectively. To present Genuity's tax provisions on a basis consistent with future periods these reimbursements have been accounted for as capital contributions. The tax provision included in the accompanying combined statements of operations represents the amounts owed for state taxes.

The significant components of Genuity's deferred tax assets and liabilities are as follows (in thousands):

	December 31, 1998	December 31, 1999
Deferred tax assets:		
Employee benefit obligations	$ 21,183	$ 22,200
NOL carryforward	24,480	24,014
Predecessor goodwill	10,241	11,830
Capitalized software	3,548	5,256
Other	14,238	13,233
Total deferred tax assets	73,690	76,533
Deferred tax liabilities:		
Depreciation and amortization	(7,100)	(32,688)
Other intangibles	(35,775)	(29,247)
Operating leases	(4,201)	(4,201)
Other	(5,308)	(2,090)
Net deferred tax asset	21,306	8,307
Deferred tax asset—current	7,604	7,785
Deferred tax asset—noncurrent	13,702	522
Valuation allowance	(21,306)	(8,307)
	$ —	$ —

The net operating losses included above relate to Predecessor and are limited in their utilization under Internal Revenue Code Section 382. A full valuation allowance has been recorded in the accompanying combined financial statements to offset the net deferred tax asset because its future realizability is uncertain.

The difference between the income tax rate computed by applying the statutory federal income tax rate of 35% to income before income taxes and the actual effective income tax rate is summarized as follows:

	1997	1998	1999
Statutory rate	(35.0%)	(35.0%)	(35.0%)
Increase (decrease) resulting from—			
State taxes, net of federal benefit	0.3	0.3	0.2
Goodwill	4.2	2.7	2.0
Meals and entertainment	0.1	0.1	—
Change in valuation allowance	6.5	(3.1)	(2.1)
Tax losses benefited to GTE	25.0	35.3	35.0
Other	(0.8)	—	0.1
	0.3%	0.3%	0.2%

11. Segment Reporting

Effective December 31, 1998, Genuity adopted SFAS No. 131, "Disclosure about Segments of an Enterprise and Related Information." SFAS No. 131 establishes standards for reporting financial information about operating segments in annual and interim financial statements and requires restatement of prior year information. Operating segments are defined as units of a business for which financial information is available that is evaluated by the primary decision-makers in determining the manner in which resources are allocated and in assessing performance of the business.

Genuity's operations are reported in three segments, Access, Hosting and Transport.

Access—Internet access pertains to a variety of global Internet access services, including dial-up, dedicated, DSL and other broadband, by providing and managing the underlying scaleable infrastructure. Genuity also provides a range of customer premise equipment necessary to connect to the Internet, including routers, channel service units/data services units, modems, software and other products. Customers receive 24 hours per day, 7 days per week network monitoring and technical support from Genuity's Network Operations Centers (NOC).

Hosting—Hosting pertains to services that allow customers to successfully implement their e-business strategies through scaleable, reliable and secure Web sites, which serve as their e-business storefronts. The e-business model enables companies to decrease sales costs; accelerate time to market; access new sales channels; increase revenues, productivity and customer satisfaction; and gain competitive advantage. Genuity currently operates ten global data centers, eight in the US, one in Leeds, England and one in Tokyo, Japan. Through the web hosting operation center, Genuity monitors these systems 24 hours a day and 7 days a week.

Transport—Genuity provides a broad range of transport services to customers through a single point of contact for planning, ordering, installing, billing, maintaining and managing our customers transport services. Genuity provides seamless operation of local loops, central office connections and interexchange carrier transport. Through Genuity's NOC, network faults, intrusion or environmental alarms are observed, diagnostics are performed, and referrals or dispatches are initiated as needed.

Other—Represents revenue from international operations and international sales of domestic operations and revenue generated from value-added Internet services of security, virtual private networks and voice over IP.

As the network, which is referred to as GNI, supports the Access, Hosting and Transport segments, it is not allocated between the Access, Hosting and Transport units for management reporting, or consequently, segment reporting purposes. Similarly, selling, general and administrative expenses are not allocated to the segments for management or segment reporting purposes.

Revenues for America Online in relation to the Predecessor's total revenues represented 54% for the six months ended June 30, 1997. Revenues for America Online in relation to Genuity's total revenues were 42%, 53% and 52% for the years ended December 31, 1997, 1998 and 1999, respectively.

Management utilizes several measurements to evaluate its operations and allocate resources. However, the principal measurements are consistent with Genuity's financial statements. The accounting policies of the segments are the same as those described in Note 1.

GENUITY INC.

NOTES TO COMBINED FINANCIAL STATEMENTS—Continued
December 31, 1997, 1998 and 1999

Financial information for Genuity's segments is as follows (in thousands):

	Predecessor	Genuity		
	Six Months Ended June 30,	Year Ended December 31,		
	1997	1997	1998	1999
Revenues				
Access	$ 94,126	$ 128,838	$ 350,777	$ 574,503
Hosting	9,601	9,690	33,469	48,811
Transport	—	65,221	72,412	89,541
Other	2,591	3,035	14,880	37,569
Total revenues	106,318	206,784	471,538	750,424
Operating Expenses				
Cost of goods sold	92,670	184,914	512,967	786,965
Selling, general and administrative	38,801	144,360	316,491	399,529
Depreciation and amortization	10,536	49,483	104,523	188,667
Total operating expenses	142,007	378,757	933,981	1,375,161
Operating Loss	$ (35,689)	$ (171,973)	$ (462,443)	$ (624,737)
Property, Plant and Equipment, Net				
Access	$ 44,212	$ 50,849	$ 100,884	$ 178,988
Hosting	7,957	23,023	29,310	52,998
Transport	—	27,313	26,752	31,706
GNI	—	263,467	704,951	1,162,287
Other	20,010	2,174	46,142	98,411
Total	$ 72,179	$ 366,826	$ 908,039	$1,524,390
Capital Expenditures[1]				
Access	$ 1,316	$ 9,544	$ 20,039	$ 97,638
Hosting	402	2,919	4,878	29,581
Transport	—	215	7,485	11,003
GNI	—	263,610	458,038	531,719
Other	1,112	23,203	97,391	80,047
Total	$ 2,830	$ 299,491	$ 587,831	$ 749,988
Depreciation and Amortization				
Access	$ 6,375	$ 6,341	$ 12,649	$ 32,543
Hosting	138	2,534	8,514	12,585
Transport	—	6,852	8,012	7,180
GNI	—	143	19,119	72,475
Other	4,023	33,613	56,229	63,884
Total	$ 10,536	$ 49,483	$ 104,523	$ 188,667

[1] Includes accruals and capital leases.

12. Commitments and Contingencies

Leases

Genuity leases office space and network equipment under long-term capital and operating leases. These leases have options for renewal with provisions for increased rent upon renewal. The Predecessor's rent expense was $2.1 million for the six months ended June 30, 1997, and Genuity's rent expense was $5.1 million, $12.9 million and $19.9 million for the years ended December 31, 1997, 1998 and 1999, respectively. Rent expense is included in cost of goods sold and selling, general and administrative expenses in the accompanying combined statements of operations.

As of December 31, 1999, future minimum lease payments under noncancelable capital and operating leases with initial or remaining periods in excess of one year were as follows (in thousands):

	Capital Leases	Operating Leases
2000	$ 33,475	$ 66,419
2001	28,701	60,143
2002	25,176	32,293
2003	11,643	26,142
2004	823	20,230
Subsequent years	—	56,502
Total minimum lease payments	99,818	$261,729
Amount representing interest	(10,128)	
Present value of minimum lease payments	$ 89,690	

GTE guarantees Genuity's existing real estate leases.

Contract Commitments

Genuity has entered into several agreements for indefeasible rights of use (IRU) for its network infrastructure in the United States. The initial terms of the IRUs are for 20-25 years, with options to extend the term. As of December 31, 1999 the outstanding commitments under the agreements is approximately $17.4 million. Genuity is also obligated to pay operating and maintenance costs under the contract terms.

In addition, Genuity has entered into a number of agreements for IRU to trans-oceanic cable systems that are either deployed or in the process of being deployed. The initial terms of the IRU is for 25 years. As of December 31, 1999, outstanding commitments under these agreements total approximately $54.4 million.

Contingencies

Some claims arising in the ordinary course of business are pending against the Company. In the opinion of management, these claims are without merit and are not expected to have a material effect on operations.

13. Related Party Transactions

Genuity recorded revenues for transport services that it provided to affiliates in the amount of $13.6 million, $17.5 million and $24.1 million for the years ended December 31, 1997, 1998 and 1999, respectively. The transport services provided are similar to services provided to unaffiliated customers and are priced at comparable rates.

Genuity purchases payroll, purchasing, electronic data processing services and other general and administrative services from affiliates whose business is the provision of these services. The cost of these services to Genuity was $39.6 million, $92.3 million and $84.1 million for the years ended December 31, 1997, 1998 and 1999, respectively, and were based on the cost of providing these services as determined by cost and time studies performed periodically.

In management's view, the cost of services provided to Genuity by affiliates reasonably approximates the costs that Genuity would have incurred if it had performed the services.

Note payable to, and receivable from affiliate include GTE funding of net cash flows to and from Genuity. Accounts receivable from, and accounts payable to affiliates represent balances from transactions in the ordinary course of business between Genuity and affiliates.

Transition Services Agreements

GTE and its affiliates currently provide a range of administrative and support services to Genuity. After the offering of Genuity's shares of Class A common stock, Genuity will enter into (1) an Agreement for Transition Services under which GTESC will continue to provide Genuity with services such as accounting and cash processing, billing and collection processing, human resource services and benefits administration and (2) an Agreement for Information Technology Transition Services under which Genuity and GTESC will provide each other with transitional information technology services.

In addition, GTESC will provide Genuity with computer programming and technical services, including the development of software interfaces and modifications and enhancements to existing systems.

Purchase, Resale and Marketing Agreement

Genuity plans to enter into a Purchase, Resale and Marketing Agreement under which Verizon will purchase services from Genuity, that will include Internet access, value-added services and private line and asynchronous transfer mode transport services. Verizon will be permitted to use the services internally or resell the services on a stand-alone basis or as part of a bundled solution. Those services resold by Verizon may be co-branded with Genuity or may be branded without use of Genuity's marks. Genuity has granted Verizon most favored customer pricing and volume-based discounts. Under the terms of the agreement, Verizon will purchase at least $500 million of Genuity's services over a five year period. In the event that Verizon has not purchased $200 million in services by the end of the third year of the contract, it would be required to pay to Genuity at that time the difference between the amount of services purchased to date and $200 million. Similarly, in the event Verizon has not purchased $500 million in services by the end of the fifth year of the contract, it would be required to pay to Genuity at that time the difference between the amount of services purchased to that date, including any shortfall payment made at the end of the third year, and $500 million.

In conjunction with the Purchase, Resale and Marketing Agreement, Genuity also plans to provide to Verizon undersea cable capacity in the Americas Region Caribbean Ring System and has committed to negotiate with Verizon with respect to obtaining capacity on the Americas III Cable Network currently under construction.

Intellectual Property Agreements

Genuity intends to enter into agreements with GTESC in order to allocate rights relating to existing and future patents, software, and technical service.

Network Monitoring Agreement

Under the terms of an existing agreement, Genuity receives continual monitoring for some elements of Genuity's network infrastructure from GTE Network Services, including monitoring of network enabling devices and processes to detect anomalies occurring in the network. The agreement may be terminated by either party on 90 days notice.

Real Estate Agreements

Genuity plans to enter into several agreements with Verizon under which Verizon will transfer to or share with Genuity various leased and owned properties including: (1) leases to Genuity of portions of specified properties owned by Genuity or Verizon; (2) subleases to Genuity of portions of specified properties leased by Verizon; and (3) assignments of leases for specified leased properties. Each agreement provides that the parties will use reasonable efforts to obtain any landlord consents required for the proposed transfer. Some of the provisions of each agreement, including the lease/sublease payment of rent term, vary depending on the underlying lease at the specified property and the result of negotiations pertaining to specific issues at a specified property.

Genuity will also enter into real estate guaranty agreements with Verizon. GTESC has agreed to either issue new or continue existing guaranties in support of our real estate obligations. The guaranties will continue until six months following the date of the offering of our shares of Class A common stock or the date on which both Standard & Poor's and Moody's publish a credit rating for Genuity, whichever occurs first. In return for the guaranties, Genuity has agreed to pay GTESC a commercially reasonable fee.

14. Subsequent Events

On   Genuity completed a recapitalization. As part of the recapitalization, Genuity converted 1,000 shares of common stock issued and outstanding to   shares of Class B common stock. In addition, GTE forgave amounts payable to GTE of $ and contributed additional capital of $.

Common Stock

The shares of Genuity's Class A common stock, Class B common stock and Class C common stock are identical in all respects, except for voting rights, conversion rights and as otherwise described below.

Voting Rights. Each share of Class A common stock and Class B common stock entitles the holder to one vote, and each share of Class C common stock entitles the holder to five votes on each matter submitted to a vote of Genuity's stockholders. Except as required by applicable law or as discussed below, the holders of the Class A common stock, Class B common stock and Class C common stock vote together as a single class on all matters submitted to a vote of Genuity's stockholders. The Class B common stockholders have the right to elect a member of Genuity's board of directors.

The affirmative vote of the holders of a majority of the outstanding shares of Class B common stock, voting separately as a class, is required for:

- any issuance of capital stock, securities convertible into Genuity capital stock or share equivalents, other than shares of Genuity's capital stock reserved at the time of the initial public offering for issuance to employees and directors pursuant to Genuity's stock option plans;
- any authorization of additional capital stock;
- any material change in the nature or scope of the business;
- any merger, consolidation, sale of all or substantially all of Genuity's assets or any similar transaction;
- any amendment to Genuity's certificate of incorporation or Genuity's by-laws that affects the rights of the holders of Genuity's Class B common stock;
- any action that would make it unlawful for a holder of Class B common stock to exercise its conversion rights; and
- any filing or declaration of bankruptcy or any full or partial liquidation.

This class vote will not be required if at any time:

- Verizon controls more than 50% of the then outstanding shares of Class B common stock and the common stock owned by Verizon and affiliates constitutes less than 10% of Genuity's outstanding common stock on an as converted basis; or
- Verizon controls 50% or less of the then outstanding shares of Class B common stock and the outstanding shares of Class B common stock constitute 50% or less of Genuity's outstanding common stock on an as converted basis;

Conversion. The Class A common stock has no conversion rights. The Class B common stock is convertible by Verizon and its affiliates into shares of Class C common stock. Prior to any exercise of the underwriters' over-allotment option, if the shares of Class B common stock were converted into shares of Class C common stock, the Class C common stock would constitute approximately 82% of Genuity's outstanding common stock, before giving effect to any issuance of shares of Class A common stock following the exercise of any outstanding employee options under Genuity's long-term incentive plans or otherwise.

The shares of Class B common stock held by any person other than Verizon or its affiliates may not be converted into Class C common stock. Instead, such shares are convertible at any time into shares of Class A common stock.

Only Verizon and its affiliates may hold Class C common stock. The Class C common stock is convertible into Class A common stock, in whole or part, on the basis of one share of Class A common stock for each share of Class C common stock. Each share of Class C common stock will automatically convert into one share of Class A common stock if at any time (1) the shares are transferred to any person other than Verizon and its affiliates or (2) the aggregate number of outstanding shares of Class C common stock, together with any shares of Class C common stock issuable upon conversion of Class B common stock, and the number of shares of Class A common stock owned by Verizon and affiliates constitute less than 10% of Genuity's then outstanding common stock.

Right to Acquire Additional Shares Upon Conversion. In limited circumstances, if Verizon holds Class A common stock and Class C common stock that in the aggregate exceed 70% of the total number of common stock outstanding at that time, Verizon may acquire from Genuity a number of shares of Class A common stock so that Verizon will own a number of shares equal to 80% of the total number of shares of common stock.

Liquidation. In the event of any dissolution, liquidation, or winding up of Genuity's affairs, whether voluntary or involuntary, the holders of the Class A common stock, the Class B common stock and the Class C common stock will be entitled to share ratably, in proportion to the number of shares they represent of

Genuity's outstanding common stock, in the assets legally available for distribution to stockholders, in each case after payment of all of Genuity's liabilities and subject to preferences that may apply to any series of preferred stock then outstanding. Genuity may not dissolve, liquidate or wind up its affairs without obtaining the consent of the holders of the outstanding shares of its Class B common stock.

Mergers and Other Business Combinations. If Genuity enters into a merger, consolidation or other similar transaction in which shares of its common stock are exchanged for or converted into securities, cash or any other property, the holder of each class of Genuity's common stock will be entitled to receive an equal per share amount of the securities, cash, or other property, as the case may be, for which or into which each share of any other class of common stock is exchanged or converted.

Other Provisions. The holders of Class A common stock, Class B common stock and Class C common stock are not entitled to preemptive rights. There are no redemption provisions or sinking fund provisions that apply to the Class A common stock, the Class B common stock or the Class C common stock.

Immediately following the closing of the initial public offering, Genuity's authorized capital stock will consist of shares of Class A common stock, par value $0.01 per share, shares of Class B common stock, par value $0.01 per share, shares of Class C common stock, par value $0.01 per share, and shares of preferred stock, par value $0.01 per share. Immediately following the closing of the initial public offering, there will be outstanding: (1) shares of Class A common stock; (2) options to purchase shares of Class A common stock; (3) shares of Class B common stock, all of which will be held of record by Verizon as of that date; (4) no shares of Class C common stock; and (5) no shares of preferred stock.

Subscription Agreement

Genuity has entered into a subscription agreement with Verizon in connection with the Class B common stock. The Subscription Agreement contains provisions requiring GTE's consent prior to taking the following agreed-upon actions:

- making acquisitions or entering into joint ventures involving cash, stock, stock equivalents or assets in excess of $100 million individually or $500 million in the aggregate during any 12-month period;
- making any dispositions of assets outside the ordinary course of business within the first two years after the initial public offering and, thereafter, making dispositions of assets in excess of $50 million individually or $250 million in the aggregate in any 12-month period;
- incurring, during any 12-month period, indebtedness that exceeds an anticipated debt level for that period to be jointly agreed upon by Genuity and GTE prior to the completion of the initial public offering;
- entering into agreements or arrangements that contain provisions that trigger a default or require a material payment when Verizon exercises its conversion right; and
- declaring extraordinary dividends or making other distributions to the holders of Genuity's common stock, including Genuity's Class A common stock.

Genuity will not be required to obtain the consent of the holders of the Class B common stock to take the above actions if at any time:

- Verizon controls more than 50% of the then outstanding shares of Class B common stock and the common stock controlled by Verizon and affiliates constitutes less than 10% of Genuity's outstanding common stock on an as converted basis; or

- Verizon controls 50% or less of the outstanding shares of Class B common stock and the outstanding shares of Class B common stock constitute 50% or less of Genuity's outstanding common stock on an as converted basis.

2000 Long-Term Incentive Plan

Genuity's employees have historically been granted options to purchase common stock of GTE. On April , 2000, Genuity's board of directors adopted the 2000 Long-Term Incentive Plan, effective immediately, which has also been approved by GTE as sole stockholder. The 2000 Long-Term Incentive Plan provides for the grant of a variety of stock and stock-based awards and other benefits, including stock options, restricted and unrestricted shares, deferred stock, stock-based performance awards and stock appreciation rights; but excluding any short-term or long-term cash awards. The 2000 Long-Term Incentive Plan will be administered by the Genuity board of directors or by the compensation committee of the Genuity board of directors. The administrator has the authority to determine eligibility, grant awards and make all other determinations under the plan.

Our 2000 Long-Term Incentive Plan provides for the grant of both incentive stock options that qualify under Section 422 of the Internal Revenue Code and nonqualified stock options. Incentive stock options may be granted only to employees. Non-qualified stock options, and all other awards may be granted to employees, officers and directors. The option exercise price of each stock option and the amount, if any, payable by participants under other awards shall be determined by the administrator, except that stock options will not be granted with an exercise price that is less than the fair market value of the Class A common stock on the date of grant. It is anticipated that Genuity will not grant existing employees any additional awards under the 2000 Long-Term Incentive Plan during the four-year period following the offering.

Options granted under our 2000 Long-Term Incentive Plan may have a term of up to 10 years. The awards are transferable to the extent, if any, determined by the administrator. The period or periods during which an award will be exercisable or remain outstanding, including any periods following termination of service, the manner of exercise and other details of awards will be determined by the administrator consistent with the 2000 Long-Term Incentive Plan.

Genuity has reserved shares of Class A common stock for issuance under the 2000 Long-Term Incentive Plan, subject to adjustment for stock splits and similar events. Concurrently with the initial public offering, the Company expects to issue options to purchase shares of Genuity's Class A common stock at an exercise price equal to the initial public offering price. The 2000 Long-Term Incentive Plan will terminate on January , 2010, unless sooner terminated in accordance with the terms of the plan.

2000 Compensation Plan for Non-Employee Directors

The 2000 Compensation Plan for Non-Employee Directors was approved by the board of directors on April , 2000 and has been approved by GTE as the sole stockholder. Pursuant to this plan, non-employee directors who have agreed to serve on the board of directors will receive, effective upon the completion of this offering, a $30,000 annual cash fee and one-time option to purchase 30,000 shares of Class A common stock at an exercise price equal to the initial public offering price. These stock options will vest in three equal installments commencing on the day of the initial public offering and on the day immediately preceding the annual meeting of stockholders in each of the next years. The administrator also has the discretion under this plan to grant options to non-employee directors in amounts and in terms as it deems is not inconsistent with the plan. Genuity has reserved a total of shares of Class A common stock for issuance under the 2000 Compensation Plan for Non-Employee Directors, of which, after taking into account the grants expected to be effective on the completion of this offering, remain available for future grants.

GENUITY INC.

SCHEDULE II—VALUATION AND QUALIFYING ACCOUNTS

For the Years Ended December 31, 1997, 1998 and 1999 for Genuity and the six months ended June 30, 1997 for the Predecessor (in thousands)

Column A	Column B	Column C		Column D	Column E
Description	Balance at beginning of period	Charged to costs and expenses	Charged to other accts.—describe	Deductions—describe	Balance at end of period
PREDECESSOR					
1997					
Allowance for doubtful accounts	$ 948	$1,840	$ 1(a)	$ (35)(c)	$2,754
GENUITY					
1997					
Allowance for doubtful accounts	$ 520	$1,898	$2,754(b)	$ (850)(c)	$4,322
1998					
Allowance for doubtful accounts	$4,322	$2,256	$ 131(a)	$(3,058)(c)	$3,651
1999					
Allowance for doubtful accounts	$3,651	$4,799	$ 201(a)	$(3,101)(c)	$5,550

(a) Represent bad debt recoveries
(b) Represents the impact of acquiring the Predecessor
(c) Represent write-offs of uncollectible receivable balances

Shares

Class A Common Stock

GENUITY

$ per Share

MORGAN STANLEY DEAN WITTER SALOMON SMITH BARNEY

PART II

INFORMATION NOT REQUIRED IN PROSPECTUS

ITEM 13. Other Expenses of Issuance and Distribution.

The following table sets forth the various expenses in connection with the sale and distribution of the securities being registered, other than the underwriting discounts and commissions. All amounts shown are estimates, except the Securities and Exchange Commission Registration Fee and the National Association of Securities Dealers, Inc. Filing Fee.

Securities and Exchange Commission Registration Fee	$ 2,640
National Association of Securities Dealers Filing Fee	1,500
Listing Fee*	*
Blue Sky Fees and Expenses	10,000
Transfer Agent and Registrar Fees	*
Accounting Fees and Expenses	*
Directors and Officers Liability Insurance	*
Legal Fees and Expenses	*
Printing Expenses	*
Miscellaneous	*
TOTAL	$ *

* To Be Included By Amendment

ITEM 14. Indemnification of Directors and Officers.

Section 145 of the Delaware General Corporation Law authorizes a court to award, or the board of directors of a corporation to grant, indemnity to directors and officers in terms sufficiently broad to permit indemnification under some circumstances for liabilities, including reimbursement for expenses incurred, arising under the Securities Act of 1933.

As permitted by the Delaware General Corporation Law, the certificate of incorporation of the Registrant provides that its directors shall not be liable to the Registrant or its stockholders for monetary damages for breach of fiduciary duty as a director, except to the extent that the exculpation from liabilities is not permitted under the Delaware General Corporation Law as in effect at the time the liability is determined. As permitted by the Delaware General Corporation Law, the certificate of incorporation of the Registrant also provides that the Registrant shall indemnify its directors to the full extent permitted by the laws of the State of Delaware.

The Registrant is in the process of obtaining policies of insurance under which coverage will be provided (a) to its directors and officers against loss arising from claims made by reason of breach of fiduciary duty or other wrongful acts, including claims relating to public securities matters and (b) to the Registrant with respect to payments which may be made by the Registrant to these officers and directors pursuant to the above indemnification provision or otherwise as a matter of law.

The Registrant has also entered into indemnification agreements with its directors and officers obligating the Registrant to indemnify its directors and officers against losses incurred in connection with claims in their capacities as agents of the Registrant. The Underwriting Agreement provides for the indemnification of officers and directors of the Registrant by the Underwriters against some types of liability.

ITEM 15. Recent Sales of Unregistered Securities.

In the three fiscal years prior to the effective date of this Registration Statement, we have issued and sold the following unregistered securities:

The sales and issuances of securities listed above, other the sales and issuances in Item , were deemed to be exempt from registration under Section 4(2) of the Securities Act or Regulation D thereunder as transactions not involving a public offering. The sales and issuances of securities listed above in Item were deemed to be exempt from registration under the Securities Act by virtue of Rule 701 promulgated under Section 3(b) of the Securities Act of 1933 as transactions pursuant to compensation benefit plans and contracts relating to compensation. All of the foregoing securities are deemed restricted securities for purposes of the Securities Act.

ITEM 16. Exhibits and Financial Statement Schedules.

(a) The following exhibits are filed herewith:

Exhibit Number	Exhibit Title
1.1	Form of Underwriting Agreement*
3.1	Certificate of Incorporation*
3.2	Amended and Restated Certificate of Incorporation (To Be Filed Prior To Closing Of Offering)*
3.3	By-laws*
4.1	Specimen Class A Common Stock Certificate*
5.1	Opinion of Ropes & Gray*
10.1	2000 Long-Term Incentive Plan*
10.2	2000 Compensation Plan for Non-Employee Directors*
10.3	IRU Agreement dated as of May 2, 1997 by and between Qwest Communications Corporation and GTE Intelligent Network Services Incorporated***
10.4	First Amendment to IRU Agreement dated as of August 13, 1997**
10.5	Second Amendment IRU Agreement dated as of May 29, 1998**
10.6	Third Amendment to IRU Agreement dated as of November 16, 1998**
10.7	Fourth Amendment to IRU Agreement dated as of February 5, 1999**
21.1	Subsidiaries*
23.1	Consent of Ropes & Gray (Exhibit 5.1)*
23.2	Consent of Arthur Andersen LLP
24.1	Power of Attorney (Signature Page)
27.	Financial Data Schedule

* To Be Filed By Amendment.

** There are portions of these agreements that have been omitted pursuant to a request for confidential treatment.

*** Incorporated by reference to the registration statement of Qwest Communications International Inc. on Form S-1/A filed with the Securities and Exchange Commission on May 16, 1997, File No. 333-25391. There are portions of these agreements that have been omitted pursuant to a request for confidential treatment.

Other financial statement schedules are omitted because the information called for is not required or is shown either in the financial statements or the notes thereto.

ITEM 17. Undertakings.

(a) Insofar as indemnification for liabilities arising under the Securities Act may be permitted to directors, officers and controlling persons of the Registrant pursuant to the provisions described under ''Item 14—Indemnification of Directors and Officers'' above, or otherwise, the Registrant has been advised that in the opinion of the Securities and Exchange Commission this indemnification is against public policy as expressed in the Securities Act and is, therefore, unenforceable. In the event that a claim for indemnification against these liabilities (other than the payment by the Registrant of expenses incurred or paid by a director, officer or controlling person of the Registrant in the successful defense of any action, suit or proceeding) is asserted by the director, officer or controlling person in connection with the securities being registered, the Registrant will, unless in the opinion of its counsel the matter has been settled by controlling precedent, submit to a court of appropriate jurisdiction the question whether the indemnification by it is against public policy as expressed in the Securities Act and will be governed by the final adjudication of the issue.

(b) The undersigned Registrant hereby undertakes that:

(1) For purposes of determining any liability under the Securities Act, the information omitted from the form of prospectus filed as part of this Registration Statement in reliance upon Rule 430A and contained in a form of prospectus filed by the Registrant pursuant to Rule 424(b)(1) or (4) or 497(h) under the Securities Act shall be deemed to be part of this Registration Statement as of the time it was declared effective.

(2) For the purposes of determining any liability under the Securities Act, each post-effective amendment that contains a form of prospectus shall be deemed to be a new registration statement relating to the securities offered therein, and the offering of these securities at that time shall be deemed to be the initial *bona fide* offering thereof.

(c) The undersigned Registrant hereby undertakes to provide to the underwriters at the closing specified in the underwriting agreement, certificates in the denominations and registered in the names required by the underwriters to permit prompt delivery to each purchaser.

SIGNATURES

Pursuant to the requirements of the Securities Act of 1933, as amended, the Registrant has duly caused this Registration Statement to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of Burlington, State of Massachusetts, on the 7th day of April, 2000.

GENUITY INC.

By /s/ PAUL R. GUDONIS
Paul R. Gudonis
Chief Executive Officer

POWER OF ATTORNEY

KNOW ALL PERSONS BY THESE PRESENTS that each individual whose signature appears below constitutes and appoints Paul R. Gudonis and Daniel L. O'Brien and each of them, his or her true and lawful attorneys-in-fact and agents with full power of substitution, for him or her and in his or her name, place and stead, in any and all capacities, to sign any and all amendments, including post-effective amendments, to this Registration Statement, and to sign any registration statement for the same offering covered by the Registration Statement that is to be effective upon filing pursuant to Rule 462(b) promulgated under the Securities Act of 1933, as amended, and all post-effective amendments thereto, and to file the same, with all exhibits thereto and all documents in connection therewith, making such changes in this Registration Statement as such person or persons so acting deems appropriate, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite and necessary to be done in and about the premises, as fully to all intents and purposes as he or she might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents or any of them, or his, her or their substitute or substitutes, may lawfully do or cause to be done or by virtue hereof. Pursuant to the requirements of the Securities Act of 1933, as amended, this Registration Statement has been signed by the following persons in the capacities and on the date indicated.

Signature	Title	Date
/s/ PAUL R. GUDONIS Paul R. Gudonis	Chief Executive Officer and Director *(Principal Executive Officer)*	April 7, 2000
/s/ CHARLES J. GIBNEY Charles J. Gibney	Director	April 7, 2000
/s/ JAMES L. FREEZE James L. Freeze	Director	April 7, 2000
/s/ DAVID B. MONAGHAN David B. Monaghan	Vice President, Finance *(Principal Financial Officer and Principal Accounting Officer)*	April 7, 2000

EXHIBIT INDEX

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EXHIBIT 23.2

CONSENT OF INDEPENDENT ACCOUNTANTS

As independent public accountants, we hereby consent to the use of our reports (and to all references to our Firm) included in or made a part of this Registration Statement.

/s/ Arthur Andersen LLP

Boston, Massachusetts
April 7, 2000